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Supreme Court of the United States

OCTOBER TERM, 1934.

No. [redacted] 1

EDWARD B. DOUGLAS,

Petitioner,

vs.

LEVI M. WILLCUTS, AS COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF MINNESOTA,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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Supreme Court of the United States

OCTOBER TERM, 1934.

No.....

EDWARD B. DOUGLAS,

Petitioner,

vs.

LEVI M. WILLCUTS, AS COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF MINNESOTA, *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.

To the Honorable Charles Evans Hughes, Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

Edward B. Douglas prays for a writ of certiorari to review the judgment of the Circuit Court of Appeals of the Eighth Circuit entered on September 10, 1934 (R. 88), reversing the judgment of the District Court (R. 64, 65). Petition for Rehearing was filed on October 8, 1934, and denied October 22, 1934 (R. 89-97).

STATEMENT OF THE MATTERS INVOLVED.

This cause involves the legality of including income of irrevocably assigned property, arising after the assignment

and received by another, in Petitioner's income for Federal income tax purposes.

QUESTION PRESENTED.

Whether the income of property, irrevocably held in a trust established by the grantor pursuant to an agreement with his divorced wife, who accepted the benefits thereof in full settlement of all interest (dower or statutory) in his property and estate and of all claim against him for maintenance and support, distributable to and received by the wife, the life beneficiary, is income of the grantor.

STATUTES INVOLVED.

Revenue Act of 1926, 44 Stat. 9, 23, 24, 32, 33, 37, 38:

Section 2, Definitions—

(a) Unless otherwise specifically provided when used in this Title—

1. The term "person" means an individual, a trust or estate, a partnership, or a corporation. * * *

9. The term "taxpayer" means any person subject to a tax imposed by this title. (26 U. S. C. A., Par. 1262.)

Section 212. (a) In the case of an individual, the term "net income" means the gross income as defined in Section 213, less the deductions allowed by Sections 214 and 206. * * * (26 U. S. C. A. 953.)

Section 213. (a) * * * The term "gross income" includes gains, profits and income derived from salaries, wages, or compensation for personal service * * *, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from

interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period. (26 U. S. C. A., Par. 954.)

Section 219. (a) The tax imposed by Parts I and II of this title shall apply to the income of estates or of any kind of property held in trust, including—

* * * * * * * * *

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, * * *;

(b) Except as otherwise provided in subdivisions (g) and (h), the tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in Section 212, except that—

* * * * * * * * *

(2) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, * * *, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under paragraph (3) in the same or any succeeding taxable year;

* * * * * * * * *

(g) Where the grantor of a trust has, at any time during

the taxable year, either alone or in conjunction with any person not a beneficiary of the trust, the power to revest in himself title to any part of the corpus of the trust, then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor.

(h) Where any part of the income of a trust may, in the discretion of the grantor of the trust, either alone or in conjunction with any person not a beneficiary of the trust, be distributed to the grantor or be held or accumulated for future distribution to him, or where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor (except policies of insurance irrevocably payable for the purposes and in the manner specified in paragraph (10) of subdivision (a) of section 214), such part of the income of the trust shall be included in computing the net income of the grantor. (26 U. S. C. A., Par. 960.)

Section 225. (a) Every fiduciary (except a receiver appointed by authority of law in possession of part only of the property of an individual) shall make under oath a return for any of the following individuals, estates, or trusts for which he acts, stating specifically the items of gross income thereof and the deductions and credits allowed under this title—

* * * * * * * * *

(4) Every estate or trust the net income of which for the taxable year is $1,500 or over;

(5) Every estate or trust the gross income of which for the taxable year is $5,000 or over, regardless of the amount of the net income; * * *

(b) Under such regulations as the Commissioner with the approval of the Secretary may prescribe a return made

by one of two or more joint fiduciaries and filed in the office of the collector of the district where such fiduciary resides shall be sufficient compliance with the above requirement. Such fiduciary shall make oath (1) that he has sufficient knowledge of the affairs of the individual, estate or trust for which the return is made, to enable him to make the return, and (2) that the return is, to the best of his knowledge and belief, true and correct. Any fiduciary required to make a return under this Act shall be subject to all the provisions of this Act which apply to individuals. (26 U. S. C. A., Par. 966.)

(Corresponding sections of the Revenue Act of 1928, 45 Stat. 791, *i. e.*, Sections 21, 22, 143, 161, 162, 166, 167, 701, 26 U. S. C. A., Pars 2021, 2022, 2143, 2162, 2166, 2701, are substantially identical with the above sections.)

STATEMENT OF FACTS.

On September 12, 1923, Petitioner, Ida M. Douglas, his wife, and Minneapolis Trust Company, a corporation, as Trustee, executed an agreement in writing (Exhibit I, R. 7 to 14) in settlement and adjustment of their respective rights and interest in the estate and property of Petitioner, whereby Petitioner assigned to Minneapolis Trust Company the securities described therein (R. 17) of an aggregate par or estimated value of $300,000 and whereby Petitioner agreed to assign additional securities of an aggregate par value of $120,000 in trust, however, to pay the income from the trust estate to Ida M. Douglas annually during her lifetime in the amount of $15,000 per annum until November 6, 1927, and in the amount of $21,000 per annum beginning November 6, 1927, and continuing during her lifetime (R. 8). The Trustee was empowered to collect the interest and prin-

cipal from the securities constituting the corpus, to reinvest the same and to make up any deficiencies in installments due and payable to Ida M. Douglas by selling securities in the trust fund, or otherwise. In the event of such a deficiency it was to request Petitioner to make good the same. It was empowered, in its discretion, to pay Petitioner, his heirs, executors, administrators, or assigns, any excess of the net income of the trust over and above the payments required from time to time to be made to Ida M. Douglas (R. 9). Petitioner waived his right to designate and determine in what securities said trust should be invested (R. 69). Ida M. Douglas accepted the provisions of the trust in lieu of and in full settlement of alimony and of any and all dower rights and statutory interests in the estate of Petitioner and in lieu of any and all claims for separate maintenance and allowance for her support (R. 10). The corpus of the trust, upon the death of Ida M. Douglas, is to be assigned to Petitioner, his heirs or assigns, and the trust then terminates (R. 12).

On September 12, 1923, Petitioner transferred to the Trustee bonds, mortgages, and corporate stocks aggregating par or estimated value of $300,000 and on December 10, 1927, Petitioner transferred to the Trustee other securities of an aggregate par value of $128,000, as provided in the agreement of September 12, 1923 (R. 15). Mr. Douglas reserved no power to revoke the trust, to revest in himself title to any part of the corpus or to control the disposition of the income thereof. No part of the income of the trust was used to pay premiums on policies of insurance on Mr. Douglas' life.

On September 15, 1923, Mrs. Douglas commenced an action of divorce against Edward B. Douglas in the District Court in and for Beltrami County, Minnesota, and on that day said court entered its judgment and decree absolutely dissolving the bonds of matrimony existing between them

and discharging them from the obligations of their marriage contract and provided that Mr. Douglas should provide and create the trust fund aforesaid and that Mrs. Douglas should have the provisions therein made in lieu of all other alimony or interest in the property or estate of Petitioner (Exhibit VII, R. 54, 55).

The net income of the trust for the calendar years 1927 and 1928 was $12,610.52 and $17,617.39, respectively (R. 58, 59). The Trustee distributed these amounts to and they were received by Mrs. Douglas in said years (R. 63, 71, 74). Mr. Douglas did not include said amounts in the net income reported by him for Federal Income Tax purposes for the calendar years 1927 and 1928. The Commissioner of Internal Revenue determined that the income of the trust for 1927 and 1928 was income to Petitioner and, accordingly, determined deficiencies in his tax of $1,758.38 for 1927 and $2,581.74 for 1928 (R. 61, 62). (Part of the deficiency for 1928 arises by virtue of the inclusion in Mr. Douglas' income of a sum representing premiums paid on policies of insurance on his life constituting part of the corpus of another trust. This part is not here in controversy.) Mr. Douglas paid the deficiencies with interest under protest and filed claims for refund, together with interest, from the date of payment. Neither claim being allowed, Mr. Douglas sued in the United States District Court in and for the District of Minnesota, Third Division, for the recovery of the amounts claimed (R. 57, 58, 62).

Said cause was submitted on December 12, 1932, to the Court, upon agreement in writing waiving a jury, and on July 27, 1932, the Court filed Findings of Fact and Conclusions of Law and its Judgment (R. 64, 65) that Mr. Douglas recover of Respondent the sums of $2,094.78 and $2,554.03, with interest as required by law on each sum from the date

of payment thereof, together with his costs and disbursements.

Respondent appealed to the Circuit Court of Appeals and his assignments of error were that there was no substantial or sufficient evidence to sustain the judgment (R. 67). The Circuit Court of Appeals, being of the opinion (R. 83-88) that the decree of the divorce court constituted an award of alimony only; that the function of the trust was to provide a method prescribed by the court for the payment of alimony only; and that the payment of alimony in this form was a legal obligation, which Petitioner was bound to meet, held, upon the authority of *Burnet vs. Wells,* 289 U. S. 670, that the income of the trust received by Mrs. Douglas in 1927 and 1928 was taxable to Petitioner because he was directly benefited by the discharge thereby of said obligation. The Court accordingly reversed the judgment of the District Court (R. 88).

SPECIFICATION OF ERRORS.

The Circuit Court of Appeals erred in holding

(1) That the income of the property assigned by Petitioner and held in trust, which was distributable and distributed to Ida M. Douglas, the life beneficiary, was taxable to Petitioner, in that such income is taxable either to the fiduciary or the beneficiary and not taxable to Petitioner.

(2) That Petitioner was legally obligated to pay alimony to his divorced wife, in that they effected a compromise and settlement whereby Petitioner's divorced wife elected to assume the position of a beneficiary or a donee.

(3) That the judgment of the District Court should be reversed, in that there is substantial evidence to support it which requires that the judgment be affirmed.

REASONS FOR ALLOWANCE OF WRIT OF CERTIORARI.

1. The Circuit Court of Appeals, in deciding that the income of the trust created by Petitioner distributed to the life beneficiary is Petitioner's income, has decided that an assignor is taxable on the income of property arising after such property has been irrevocably assigned, although the assignor has relinquished the right to demand and obtain the income and control it after its receipt, and thus has decided an important question of Federal law which has not been but should be settled by this Court.

   (a) The income taxed to Petitioner is income of property held in trust and taxable to the fiduciary or the life beneficiary under Sections 219, Revenue Act of 1926, and 161 and 162, Revenue Act of 1928, *supra*.

   (b) Neither *Burnet vs. Wells*, 289 U. S. 670, nor the doctrine that the amount of a legal obligation assumed and paid by an assignee of property is taxable income to the assignor, which controlled the view of the Circuit Court of Appeals, is applicable.

2. The Circuit Court of Appeals, in deciding that the income of property irrevocably held in a trust established by the grantor pursuant to an agreement with his divorced wife, who accepted the benefits thereof in lieu of her interest (dower or statutory) in his property and estate and right to maintenance or support, distributable to and received by the wife, the life beneficiary, has decided that the divorced wife has not voluntarily elected to assume the position of a beneficiary or a donee and, thus, it has decided a question of

Federal income tax law in a way which is in conflict with applicable decisions of this Court.

3. The Circuit Court of Appeals, in deciding that Petitioner is taxable on the income of the trust created by him, distributable and distributed to the life beneficiary, has decided that, although property is irrevocably assigned and the assignor has irrevocably relinquished the right to demand and obtain the income thereof and control it after its receipt, the assignor is taxable on the income arising after the assignment and has thus rendered a decision in conflict with the decisions of other Circuit Courts of Appeal on the same matter.

WHEREFORE, your Petitioner respectfully prays that a writ of certiorari issue to the United States Circuit Court of Appeals for the Eighth Circuit and submits his brief hereto attached in support of this petition.

Respectfully submitted,

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